

**THE ROLE OF KENYA INVESTMENT AUTHORITY IN
ATTRACTING FOREIGN DIRECT INVESTMENT IN KENYA**

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**A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF
THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF
MASTER OF BUSINESS ADMINISTRATION**

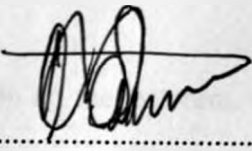
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OCTOBER, 2011

DECLARATION

This Research project is my original work and has not been presented for examination in any other University.

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This research project has been submitted for examination with my approval as university supervisor.

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ACKNOWLEDGEMENT

This research project report could not have been possible without the support and cooperation of my ever devoted supervisor; Dr. John Yabs without whom the quality of this document would not be satisfactory. His guided corrections and suggestions significantly enhanced the eminence of this document.

I am grateful to all the lecturers, relatives and friends who kept on encouraging me to put in more effort throughout the course. Predominantly, I appreciate my workmate and departmental head, Catherine Naliaka Mbotela who relentlessly followed up on my progress with constant words of encouragement, and Dr. Monicah Musyoka, who instilled into me the hope and persuasion to move on against all odds in the course of the schoolwork. Am equally indebted to the staff of Kenya Investment Authority who participated in this study. In addition, special tribute goes to Reuben Musyoki and Mwanasudi Bakari for leading the data collection process.

Finally, my heartfelt appreciation goes to my own father and mentor Mr. John Munyoki Kirai for his unremitting guidance in life and for believing in me, and for my mom Mary Mutave Munyoki who always ceaselessly prays for me. Above all, to the Almighty God for giving me good health and the otherwise necessary provisions in the period of my studies up to now.

DEDICATION

I dedicate this work to my dear wife Dorcas Mwende Caleb, my lovely daughters Rehema Muthu Caleb and Natalia Mumbi Caleb, and to my son and mentee, Prince Kittonga Caleb, for their earnest support, motivation and love, and for bearing with me during the long hours of absence as I attended to my studies.

ABSTRACT

Foreign direct investment is important in a developing country where there exist a high level of unemployment and generally a need to improve the livelihood of the people. In this context therefore, there is need for a country to develop a conducive business environment that will attract the same the foreign investors and establishment of one stop shop where all enquiries pertaining to both local and foreign investment in the country will be available, is such one step. The study aimed at establishing the role of Kenya Investment Authority in attracting direct foreign investment in Kenya.

Towards the realization of the same objective, a case study research design was adopted whereby the researcher interviewed five managers in KIA. The respondents had different academic qualification and years of experiences in dealing with implementation of the institutions strategies for attracting direct foreign investment in the country. The data was collected through the use of the interview guide that was prepared to guide the researcher on the research objective.

The findings of the study were that Kenya has increasingly become attractive to FDI in the last 10 years and this has been due to an improved road and telecommunication infrastructure as well as more recently the enactment of a new constitution that has put more safeguards in the protection of private property and thus no individual government can take a seizure policy without contravening the law. KenInvest facilitates approvals of prospective investment projects which have their details submitted on a prescribed application form issued by KenInvest. KIA has provided one-stop shop advantage office for investors in that all issues pertaining to local investment can be found in the office. In addition, KIA has developed a code that set forth guidelines on investment that enumerate the various investment incentives and mandate that all new projects should obtain before approval is granted. In addition, the interviewees observed that KIA has been continuously

lobbying the government to harmonize investment regimes in all the East African Community countries and which will eventually aim to remove all tariff barriers between the states.

Attraction of direct foreign investment to a country is of importance in terms of creating employment and increasing the general economic development of the country. Therefore, it is important that a country establishes all necessary mechanism that will attract these investors. The necessary conditions such as efficient communication and road network should be availed and the cost of production also are made affordable through a supply of affordable labor, raw materials and power for running the factories.

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CHAPTER ONE: INTRODUCTION

1.1 Background to the Study

Governments of developing countries are now giving new attention to the potential for foreign direct investment (FDI) in their economies. This is because many developing countries now desire to extend the market price system and the private sector and to mitigate the external debt problem by attracting more private foreign investment (UNCTAD, 2002). The Government is responsible for the formulation and implementation of laws that will ensure that the country attracts foreign investors by ensuring that they operate in an environment which is better than other countries. This involves ensuring that the number of licenses needed to operate is few, and the duration it takes to grant the licenses is minimal. This results from the institution operating in an environment where it is committed to transparency and fiscal decentralizations tasked with granting the license being few (Graham, 2006). During the past two decades, foreign direct investment (FDI) has become increasingly important in the developing world, with a growing number of developing countries succeeding in attracting substantial and rising amounts of inward FDI.

According to Hennart (1982), in the imperfect market argument based on transaction cost theory, market imperfections arise due to barriers such as tariffs and foreign exchange controls that restrict the free flow of goods between nations. To avoid such barriers, it is better for MNCs to move abroad through FDI instead of exporting or licensing its products. Furthermore, the transaction costs of exporting or licensing are much higher since the MNCs may incur costs of search, costs of negotiation, costs related to enforcement of contract, transport cost and payment of taxes (Hill,

2001). These justify the reason for shifting production abroad. Globalization is formed and fashioned in and through particular political economies and techno-economic relations. Additionally, globalization is characterized by structural reforms such as trade and investment liberalization and increased trade and international investment flows promoting growth, altering the composition and geographical distribution of economic activities, stimulating competition and facilitating the international diffusion of technologies having significant effects, both positive and negative, for sustainable development (Vernon, 2005). Multinationals are the vehicles for much of this globalized economic activity, and in turn, foreign direct investment by multinational corporations accounts for an increasing proportion of global economic activity. The escalation in international investment means that a country's sustainable development is progressively more influenced by multinational enterprises (MNEs) (Larrain et al., 2001).

1.1.1 Foreign Direct Investment

A foreign direct investment (FDI) is defined as an investment involving a long term relationship and reflecting a lasting interest and control of a resident entity in one economy in an enterprise resident in an economy other than that of the foreign direct investor (UNCTAD 2002). An equity capital stake of 10% or more of the ordinary shares or voting power of an incorporated enterprise, or its equivalent for an unincorporated enterprise, is normally considered as a threshold for FDI. Foreign direct investment, in its classic definition, is defined as a company from one country making a physical investment into building a factory in another country. The direct investment in buildings, machinery and equipment is in contrast with making a portfolio investment, which is considered an indirect investment (UNCTAD 2002).

Foreign direct investment (FDI) plays an extraordinary and growing role in global business. It can provide a firm with new markets and marketing channels, cheaper production facilities, access to new technology, products, skills and financing. For a host country or the foreign firm which receives the investment, it can provide a source of new technologies, capital, processes, products, organizational technologies and management skills, and as such can provide a strong impetus to economic development (Lim, 2002). In recent years, given rapid growth and change in global investment patterns, the definition has been broadened to include the acquisition of a lasting management interest in a company or enterprise outside the investing firm's home country. As such, it may take many forms, such as a direct acquisition of a foreign firm, construction of a facility, or investment in a joint venture or strategic alliance with a local firm with attendant input of technology, or even licensing of intellectual property. In the past decade, FDI has come to play a major role in the internationalization of business. Reacting to changes in technology, growing liberalization of the national regulatory framework governing investment in enterprises, and changes in capital markets profound changes have occurred in the size, scope and methods of FDI (Hennart, 1982). New information technology systems, decline in global communication costs have made management of foreign investments far easier than in the past. The sea change in trade and investment policies and the regulatory environment globally in the past decade, including trade policy and tariff liberalization, easing of restrictions on foreign investment and acquisition in many nations, and the deregulation and privatization of many industries, has probably been the most significant catalyst for FDI's expanded role.

1.1.2 Kenya Investment Authority

The Kenya Investment Authority is the successor institution to the Investment Promotion Centre, which was established in 1986 with the primary role of attracting and retaining local and foreign

direct investment in the country. The main functions of the Centre were to, Promote investments in Kenya by local and foreign business enterprises, Liaise with the relevant Ministries, responsible for approving all new private sector projects and expansion of existing projects, Assist business enterprises in implementing projects approved by the relevant Ministries, Monitor the performance of the projects approved by the relevant Ministries and compliance with the conditions of approval and advise the government periodically on changes in policies, strategies and administrative procedures necessary for the promotion and enhancement of investments in Kenya

In 1992, the Centre was vested with the power to issue a Certificate of General Authority (GA) in respect of any new business enterprise, upon the application of any person proposing to invest in or establish that enterprise. The GA was introduced to reduce the bureaucracies involved in acquiring the various licenses that an investor required in setting up a project. It entitled an investor to start his project immediately, provided that any licenses he required were covered by the GA, and were subsequently acquired within twelve months. However, as there were a number of different laws that dealt with or had an impact either directly or indirectly on foreign investments, it was decided after wide consultations, that Kenya needed a legal framework contained in a single piece of legislation that specifically and substantively covered the matter of direct investment in the country. This would not only give greater clarity in dealing with investments into Kenya, but would also give transparency and confidence to investors.

Consequently, after years of intensive and interactive consultations, the passing of the Investment Promotion Act on December 31st, 2004 created the Kenya Investment Authority, with an expanded mandate under the Act in executing its role of investment promotion, investment facilitation and

policy advocacy. The key features in this regard include: The power to issue an Investment Certificate (which replaced the Certificate of General Authority) with regard to any new investment, upon satisfying requirements for the same. It is optional for both foreign and local investors and the Authority is expected to give a written decision within 20 working days, after receiving an application for an investment Certificate, Re-modeling the Authority into a one-stop shop for investors, as per the Investment Program of the Economic Recovery Strategy 2004, thereby significantly raising its profile and responsibilities, and the expectations of investors for more efficient service delivery and the power to determine whether an investment is lawful and beneficial to Kenya. To date, KIA has had mixed fortunes in the execution of its mandate under the Investment Promotion Act.

1.2 Research problem

The impact of FDI on economic growth is one of the most controversial topics in development economics. According to the modernization hypothesis, FDI promotes economic growth by providing external capital and through growth, spreads the benefits throughout the economy (Contractor et al., 2003). It is the presence, rather than the origin of investment that is considered to be important. Moreover, FDI usually brings with it advanced technology, and better management and organization which can be considered as the engine of the growth in developing countries. However, despite the role that foreign direct investment plays in the economies of the countries, it has been noted that that often than not cumbersome and bureaucratic administrative regulations has been noted to affect the flow of FDI especially in the developing countries (Erdal, 2001).

Kenya Investment Authority aims at setting up a One Stop Shop to foreign investors in which an investor deals with one single institution to obtain all the necessary documentation in one streamlined and coordinated process. The operation of this would thereby reduce the number of bureaucratic procedures that hamper investment flows through increased costs and time wasted. Key departments which constitute the One Stop Shop would be brought under one roof within the auspices of the Investor Services Division. The main functions of the Centre include the promotion of local and foreign enterprises, liaising with relevant ministries, assisting business enterprises in implementing projects approved by the relevant Ministries among others. With the fulfillment of this role then investor can then rely on the Authority to provide virtually all the approvals and clearances required to set up a business. Despite the improved licensing requirement in the country, investors have continued to complain of the level of licenses required in setting up businesses locally. They still suggest that all unnecessary and bureaucratic licenses to be done with in order to make the country an investor friendly destination.

Several studies have been undertaken locally in the subject area of foreign direct investment. Dinga (2009) undertook a study of the impact of foreign direct investment on economic growth in Kenya. He found out that foreign direct investment provides a source of new technologies, capital, processes, products, organizational technologies and management skills, and as such can provide a strong impetus to economic development. On his part Njuguna (2009) carried out a study on the factors that influence the contribution of foreign direct investment in the growth of Telecommunication sector in Kenya. In this study he did note that few and easy to achieve licensing procedures in a country plays an important role in attracting FDI in the country. Iseme (2008) in his part researched on an empirical study of location determinants of foreign direct investment in Kenya. He found out that there exist a strong relationship of around 72% between a

location of a country and the foreign direct investment in that country. On the basis of the above studies, it is evident that there has been no study that the researcher is aware of on the role of the licensing process on foreign direct investment, a case of Kenya Investment Authority. This therefore leads to the following research question; what role does Kenya Investment Authority play in attracting foreign direct investment in Kenya?

1.3 Research objectives

The objective of the study was to establish the role of Kenya Investment Authority in attracting foreign direct investment in Kenya.

1.4 Value of the study

The study will help the management of the Kenya Investment Authority to come up with clear guidelines on the procedure which an investor needs to follow when seeking the license and also on the need to reduce the number of licenses which the investor needs to have in order to operate. In this way it will reduce the time it takes for an investor to acquire the license.

To the government: This study will benefit the government especially the Ministry of Finance and that of Trade in making policy decisions whose overall objectives are to accelerate the rate of growth in the amount of foreign direct investment and take advantage of the growing world markets.

The study will be important to the scholars as the study will increase to the body of knowledge in this area and also they can offer advice to the government on what if done will attract more foreign direct investment to the country.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter provides an overview of the previous literature on foreign direct investment. An overview of the various theories underlying foreign direct investment, factors influencing foreign direct investment and the licensing process will be reviewed.

2.2 Theories of Foreign Direct Investment

According to the imperfect market argument, which is based on transaction cost theory, MNCs should internalize their operations (Hymer, 1976 & Hennart, 1982). According to this theory, market imperfections arise due to barriers such as tariffs and foreign exchange controls that restrict the free flow of goods between nations. To avoid such barriers, it is better for MNCs to move abroad through FDI instead of exporting or licensing its products. Furthermore, the transaction costs of exporting or licensing are much higher since the MNCs may incur costs of search, costs of negotiation, costs related to enforcement of contract, transport cost and payment of taxes (Hill, 2001). These justify the reason for shifting production abroad. Logically, a multinational corporation (MNC) is bound to incur additional transportation costs, face language and tax barriers and may face the risk of expropriation if it decides to move abroad. However, Dunning (1991) observe that MNCs are still rapidly crossing borders and expanding their businesses all over the world through FDI.

The product life cycle theory by Vernon (2005) argues that the production location for products moves from one country to another depending upon the stages of the product's life cycle. In other words, MNCs undertake FDI in other countries once demand there grows large enough to support local production and the domestic market is saturated and facing rising cost of labor. However,

Hill (2001) argues that if this is the case, it still does not explain why MNCs use FDI and not exporting. According to the ownership advantage theory where MNCs are fully exploiting certain intrinsic competitive advantage that the local firms may not have (Caves, 2002). These advantages refer to certain technological advantages including superior production techniques, better management methods, brand name, reputation, benefits of economies of scope and scale, monopolistic advantage and ownership of scarce resources (Hill, 2001). These factors are also known as firm specific advantages.

According to the Locational advantage argument provided by Dunning (2005) that explains the nature and direction of FDI based on certain locational factors. MNCs carry out their FDI due to certain locational factors inherent in the host market. These locational factors are further divided into demand factors and supply factors (Coskun, 2001). The demand factors are: large market, high domestic demand, openness of the economy, potential growth, etc. while the supply factors are cheap and skilled labor, infrastructure quality, government incentives, logistic cost, access to technology, etc. The Multimedia Super Corridor (MSC) in Malaysia is an example of an area with certain locational specific advantages since it attracts concentration of information and technological companies that conduct research. These factors are also known as country specific advantages.

Knickerbocker (2003) Follow the competitor theory argues that, FDI flows are a reflection of strategic rivalry between firms in the global marketplace. He examined the relationship between FDI and rivalry in the oligopolistic market structure and found that there is a tendency for firms to follow the leader. In the service sector, this is evident when service firms internalize as a reaction to competing firms. Coskun (2001) in the investigation of Swedish banks found that there is a tendency for them to follow the leader when competing in a foreign market. However, Hill (2001)

argues that this theory still does not explain why the leader decides to go abroad through FDI rather than exporting.

On their part, Contractor et al (2003), Follow the client theory is another theory that gathered momentum in the 80s and tried to explain the expansion of service based MNCs. According to this theory, advertising, financial services and market research companies tend to follow their multinational-manufacturing clients abroad. According to Erramilli and Rao (2003), it seems that from the 1980s onwards, knowledge based service sectors tended to expand internationally using the follow the client theory when they followed their multinational clients abroad.

2.3 Foreign Direct Investment

According to United Nations Conference on Trade and Development (UNCTAD) (2002), foreign direct investment FDI is an investment involving a long term relationship and reflecting a lasting interest and control of a resident entity in one economy in an enterprise resident in an economy other than that of the foreign direct investor. An equity capital stake of 10% or more of the ordinary shares or voting power of an incorporated enterprise, or its equivalent for an unincorporated enterprise, is normally considered as a threshold for FDI.

Foreign direct investment has played an effective role as a source of financing to a lot of developing countries. Although the impact of FDI on economic development is debatable, there are many empirical findings that support its positive contributions. Research by Mbekeani (1999) on the impact of FDI on domestic investment, exports and economic growth showed positive relationship in Mexico and Malaysia. Another research by Larrain, Luis and Andres (2001) showed positive effect of FDI generated by Intel in terms of net exports, investment, wages and benefits and local purchases for the Costa Rican economy. Hill (2001) in his study on the role of

FDI in 69 developing countries found that it not only stimulates economic growth but also has a larger impact than investments by domestic firms. Developing countries are thus, competing to attract FDI into their economy. There are many factors that attract the movement of FDI throughout the world. These factors may differ significantly from one location to another depending again on the attractiveness of the particular region or country.

2.4 Factors influencing foreign direct investment

A number of studies have been undertaken to explain the various factors that influences foreign direct investment. The factors identified include; locational factors (country specific factors), and ownership factors.

2.4.1 Locational Factors

Market size or market attractiveness can be assessed or measured by examining host country's GDP, population growth of GDP, GDP per capita, etc. Empirical evidence investigating market size and attractiveness in the host country as a variable influencing FDI has shown mixed results although most findings support the theoretical view that large markets attract FDI (Anand and Kogut, 2007). Galan and Benito (2001) in their research on the determinants of FDI in manufacturing and service companies in Spain found that growing demand in the host market and the large size of the market as important determinants of FDI. Why does market attractiveness enhance inward FDI? According to Hasan (2004) in his exports are crucial determinant in attracting investment. He found out that a 1% rise in exports is likely to increase FDI inflow by around RM120 million. So, for manufacturers, growth of exports is thus an important factor to influence foreign investors confidence. Hasan (2004) further reiterates that FDI tends to boost exports from home country to host country and imports from host country to home country. If this



is the case, then market size may not be so important for manufacturing MNCs as compared to service MNCs. Service MNCs as mentioned above are mostly not export oriented and therefore depend heavily on local market for sales.

The size of the foreign market and its potential growth are regarded as key factors influencing choice of location (Knickerbocker, 2003). Furthermore, proximity and access to a free trade area are also key factors, and as such, the size and growth of the larger, free trade area may be more important than the size and growth of the particular country in which the firm has chosen to invest.

In addition, increased knowledge of a foreign country reduces both the cost and uncertainty of operating in a foreign market (Buckley and Casson, 2005). Related to knowledge is experience which is thought to provide important tangible and intangible advantages (Buckley, 2005). Again it is generally believed that a firm with greater experience of a particular location is more likely to invest there than a firm with less experience (Anand and Kogut, 2007). Although financial incentives have been studied extensively for their effect on investment decisions, it is generally concluded that they have relatively little impact on location choice (Tatoglu and Glaister, 2008). Furthermore, it has been noted that FDI can be quite shallow and therefore transient if the investors are attracted merely by financial inducement rather than by fundamentals such as skilled labour (Dunning, 1991).

A transaction cost approach has been frequently employed to explain why firms own and control operations in foreign markets. Stemming from this is the cost minimization school of thought, which implies that a company will choose the lowest cost location for its production activities abroad (Buckley, 2005). While transport and raw materials are undoubtedly key cost factors, it is the cost of labor that has been explored most extensively in the FDI literature. However, previous

research has produced mixed findings. Some studies have reported that higher wages reflect a more productive workforce and, as such, are associated with increased foreign investment (Buckley and Casson, 2005). On the other hand, some research reports the reverse effect, supporting the cost minimization theory (Knickerbocker, 2003).

The availability of resources, in particular labor and raw materials, are widely acknowledged as influencing a firm's FDI decisions (Dunning, 1991). In terms of labor, population density (Knickerbocker, 2003) and unemployment rates (Knickerbocker, 1999) have been found to influence inward investment. With regard to raw materials, many overseas subsidiaries rely on local suppliers for some standard inputs. However, it is thought that, more recently, availability of raw materials has had relatively less impact since raw materials are already often sourced on a global basis (Buckley and Casson, 2005).

Access to technology has been regarded as an influencing factor in investment location and specifically the ownership level of the investing firm, as mentioned previously (Erramilli *et al.*, 2003). Bernama (2004) warns that even if a country has a high level of research and development expenditure, this may not be due to a high level of technological dynamism across the board but rather the result of a structural leaning towards industries with high research intensities. This bias will be mitigated only to the extent that industry structures between advanced countries tend to be fairly similar. In the context of FDI, political stability or risk pertains to the risk that a host government will unexpectedly change the “rules of the game” within which businesses operate (Kravis & Lipsey 2002). It also incorporates the risk of adverse consequences arising from political events.

Workforce factors refer to variables such as cost of labor-wages, education level, skill level, etc. Empirical evidences from variables investigated found mixed results. For example, Globerman and Shapiro (2009), Jenkins and Thomas (2002), and Kravis and Lipsey (2002) found in their empirical investigation that wages are negatively associated with FDI. In the Malaysian scenario, some service industries such as banking, insurance, information technology, telecommunication and BPO are capital and knowledge intensive. These industries depend on semi-skilled and educated labour. Malaysia is able to supply such workforce at relatively lower cost compared to established service economies such as Singapore. That is why, this sector still attracts a substantial amount of FDI. Furthermore, there may be other factors such as availability of high quality English speaking, educated work force which is highly important in the services sector. A report by Bernama (2004), said that Shell's success in Malaysia was largely due to the availability of cheap, highly talented, highly trainable and capable Information Technology (IT) workforce. However, in certain services sector, such as the hypermarket retailing business, cost of manual labor may be more relevant since this sector employs unskilled workforce. So, whether cost of labor is an important determinant may depend on the type of service industries under consideration.

In addition, government variables such as government incentives, economic policies, political environment and government promotions towards FDI influences the level of direct foreign investment in a country. Theoretically, the tax regime is expected to have an inverse relationship with FDI (Kerr & Peter, 2001) i.e. lower taxes promote FDI and vice versa. The same goes with the openness of an economy. It was found that the more open an economy, the higher FDI it attracts (Kerr & Peter 2001). They also found out that tax incentives had a positive effect on FDI. The degree of openness was also found to have positive impact on FDI in many studies. Kravis

and Lipsey (2002) also found the degree of openness as measured by the high propensity to trade as an important factor influencing FDI.

2.4.2 Ownership factors (Firm specific factors)

MNCs ownership advantages can also influence FDI. MNCs owning a valuable asset that creates a competitive advantage in the home country can use that advantage to venture into markets abroad (Jenkins & Thomas, 2002). The ownership advantages include experience effects, firm expertise, reputation/brand image and size of the firm.

Buckley (2005) had shown that American MNCs proceed abroad gradually, where initially they go to familiar markets that are close. As soon as they gain more experience, they move on to unfamiliar markets that are geographically distant. Buckley (2005) showed that experience had a positive effect on FDI. In the service industries such as advertising, Gabriel (2007) also observed experience effects influencing FDI. As advertising MNCs grew in size and obtained more experience, they started to penetrate into Europe and Latin America. Erramilli (2003) found that as service MNCs obtained more experience, they tended to choose markets that are culturally less similar to home country. Gabriel (2007) on the internationalization of professional business services found a positive relationship between intention to internationalize and age of the firm. In other words, older and more experienced firms tend to internationalize faster. Even in the internationalization of hotels, the experience effect was observed (Dunning & McQueen, 1991). They found that large hotels that are more diversified and experienced could enter new markets easily since they enjoy economies of scale and have vast managerial and organizational expertise.

Jenkins and Thomas (2002) in their research on FDI in the insurance industry found that intellectual property right is an ownership advantage that needs to be protected when expanding

abroad. Vernon (2005), in his empirical investigation also showed that technology is a key determinant of the supply of insurance services by MNCs. Galan and Benito (2001) in their research on Spanish financial companies found that they stressed the importance of specific and intangible assets such as technology, innovative capability and managerial expertise as their ownership advantage. However, they found that economies of scale do not influence FDI of Spanish financial institutions. Kravis and Lipsey (2002) found that technological assets of US MNCs have positive influence on FDI.

Larrain et al., (2001) in their studies of manufacturing industries found that large firms are more likely than small firms to be foreign investors. Firm size was found to show positive impact on the internationalization of banks and advertising firms (Tatoglu & Glaister, 2008). In the case of the Malaysian services sector, variables such as reputation, experience effect, brand image, and size of the firm are considered to be important for MNCs. For example in the banking industry, some of the foreign banks in Malaysia such as HSBC and Standard Chartered have been in operation for more than a century and also have presence all over the world. Their reputation, experience and size may definitely give them an edge over new players in the industry. However, this may not be true for new and small service MNCs.

2.5 Licensing of foreign direct investment

According to UNCTAD (2002) African countries have generally simplified their procedures for entry of FDI since the early 1990s. FDI is no longer routinely screened in most countries, and some now apply policies of guaranteeing a transparent registration of projects meeting proper criteria. However, many countries still impose general restrictions on entry, either by prohibiting foreign investment below a certain size, through minimum capital investment or by requesting prior

approval or licensing from which domestic investors are exempted. Previous restrictions on foreign purchase of domestic shares (in capital markets) have been relaxed in several countries. Without prejudice to restrictions on FDI laws, non-residents are now in principle allowed to own up to 100 per cent of domestic enterprises in all the countries under review, except in Ghana, Kenya and Mauritius where foreign ownership cannot exceed a fixed threshold (Gabriel, 2007).

By accepting the obligations of the of the IMF's to remove restrictions on payments and transfers for international current transactions, and to adopt multilateral payment system free of restrictions and discriminations, these countries opened up their markets to the outside world, Coskun (2001). Most countries have put rules in place guaranteeing investors an unrestricted remittance of dividends, profits and liquidation proceeds, on condition that payment of taxes and other liabilities has been made according to local regulations. Most of African countries have retained restrictive practices toward some specific categories of FDI. They discourage foreign investment in certain sectors either to stimulate local entrepreneurship, to protect sectors deemed to be of strategic interest, or to maintain the monopoly position of state enterprises (Jenkins & Thomas, 2002). As a general rule, the majority of countries tend to discriminate against foreign investors in activities judged to be particularly suited to national or local entrepreneurs; such practices are found in sectors like small-scale manufacturing and mining, some trading activities and proximity services. Foreign participation in financial services is restricted and/or subject to more burdensome licensing requirements than applied to domestic investors in six countries. The other countries do not report discriminatory regulation against foreign entrepreneurs wishing to invest in financial activities. More generally, progress has been made in transferring financial services from the public to the private domain (Anand & Kogut, 2007).

To boost local entrepreneurship and self employment, most governments ban or restrict foreign participations in certain kinds of other services, especially the ones that do not call for specialized expertise, (Lipsey, 2002). In the primary sector foreign entrepreneurs are in most cases not allowed to invest in small scale mining, in construction companies and in some agricultural activities. Furthermore, regulations also deny national treatment to non-domestic entrepreneurs wishing to invest in the manufacturing sector in many countries. In most countries land is either officially owned by the state, or has various kinds of ownership status, and its purchase is restricted to nationals (Hennart 1982). Foreign investors can acquire the right to use land only through leasehold contracts, generally renewable, but not exceeding 99 years in total. In addition, the extensive network of government agencies and traditional communities involved in granting land rights and, in some countries, problems with identifying the true owners of a piece of land, raise the costs, risks and administrative burden on foreign investors.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter discusses the research methodology that was used in the research. The chapter adopted the following structure: the research design, target population, and data collection methods and data analysis method to be used.

3.2 Research design

The research design was a case study. A case study is an in-depth investigation of an individual, institution or phenomenon. The primary purpose of a case study is to determine factors and relationships among the factors that have resulted in the behavior under study. The research study was adopted in this particular study since not all the target population of the study were knowledgeable of the role of the licensing process on the foreign direct investment. In light of this therefore, a case study design was deemed the best design to fulfill the objective of the study as the results were expected to provide an insight in the role of KIA in attracting direct foreign investment. It is through an interview with some selected persons concerned with developing and regulating the process of FDIs that the research objective could be obtained. The interviewees were the managers and functional heads in Legal, Liaison, Human Resources, and Licensing department. These were considered to be key informants for this research. As a result of this, a case study research design was deemed an appropriate design.

3.3 Data Collection

The study made use of primary data which was collected through a face to face interview with the researcher. An interview guide was used to collect data on the role of KIA in attracting direct foreign investment in Kenya. The interviewees were those involved with formulation, evaluation and implementation of the strategies in attracting foreign investors. The interview guide was made up of three sections namely; respondents profile, business environment in Kenya and the role of Kenya Investment Authority in attracting foreign direct investment. The researcher believes that this made it possible to obtain the data required to meet specific objectives of the study. The interviewees were the managers and functional heads in Legal, Liaison, Human Resources, and Licensing department. These were considered to be key informants for this research.

3.4 Data Analysis

The data obtained from the interview guide was analyzed qualitatively. Qualitative data analysis makes general statements on how categories or themes of data are related. The qualitative analysis was adopted in this study because the researcher was able to describe, interpret and at the same time criticize the subject matter of the research since it will be difficult to do so numerically. The qualitative analysis was done using content analysis. Content analysis is the systematic qualitative description of the composition of the objects or materials of the study. It involves observation and detailed description of objects, items or things that comprise the object of study. The themes (variables) that were used in the analysis were broadly be classified into two: foreign direct investment and the role of KIA in attracting direct foreign investment in the country.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

The research objective was to establish the role of Kenya Investment Authority in attracting foreign direct investment in Kenya. This chapter presents the analysis and findings with regard to the objective and discussion of the same.

4.2 Respondents Profile

This part of the interview guide was intended to assess the capacity of the respondents to answer the questions on the interview guide and also whether they are versed with the subject matter of the study. The research aimed at interviewing five senior managers at Kenya Investment Authority that are involved in the formulation, evaluation and implementation of the policies that affect the level of foreign direct investment. The specific respondents in the interview were the Licensing manager, Human resource manager, Liaison manager, investment manager and the communication manager. All the five respondents were available for the interview. And there 100% response rate was achieved. The respondents had different academic backgrounds ranging from Finance, Human Resources, Communication, Investment and Law. Three of the respondents had in addition undergone further training in foreign countries and attended seminars that were organized by regional trading blocs such as Comesa, EAC and SADC to enhance their capacity in handling foreign investment matters. In addition, the views of both genders were represented by the respondents interviewed because two of the respondents were female. This meant that the views expressed by the respondents were not gender biased. With such academic and professional background the respondents were deemed to be capable to correctly establish the role of KIA in attracting foreign direct investment.

The work experience for the respondents ranged from two and half years to ten years both within the organization and without. On average, the respondents had worked in the organization for four years. Having worked in the organization for such a period, the researcher believes that the respondents will have firsthand experience on the role KIA in attracting direct foreign investment in the country. Generally with this solid background in form of the respondents academic qualification and work experience, it was felt that the respondents were knowledgeable enough on the research subject matter and thus of help in the realization of the research objective.

4.3 Foreign Investment Environment in Kenya

This section of the interview guide wished to establish from the respondent what the current foreign direct investment climate in the country is like. This position will help to assess whether the Kenya Investment Authority is currently able to play its rightful role of attracting foreign investors in the country.

All the respondents pointed out that indeed the current business environment has improved in Kenya over the last ten years. They observed that prior to the year 2002; the country had lagged behind other regional countries in terms of being a destination of foreign investors. As to the reason why the same has changed, the respondents noted that foreign investors majorly are concerned with the operating cost of their businesses and as well as the security of their investment. They pointed out that the cost of investment will come in form of efficiency of the country's communication infrastructure, labor cost, inflation and source of raw material. As a result of the same, the interviewees acknowledged that prior to the year 2002, the state of our roads was so much dilapidated, communication was wanting and the political environment was in a state of uncertainty. Three of the respondents noted that at some time in 2001, the rate of

inflation stood at 22% and at such a level, no investor will wish to put his/her money in such a climate because its returns will be eaten up by the inflation and even the capital invested. However, the interviewees noted that over the same period, the country has been able to attract over \$2.3 billion worth of direct foreign investment majorly in the telecommunication sector. In addition, the respondents pointed out also that in the year 2010/2011, Kenya's total FDI stood at Sh. 143.9 billion though it had dropped by Sh. 100b from the previous year. The highest recorded foreign direct investment though was in 2008/2009 when the country attracted Sh. 163.4 billion.

Further, the respondents observed that with the enactment of the new constitution in the country, private property has been safeguarded from the state and thus no individual government can take a seizure policy without contravening the law. This they observed will help in attracting more direct foreign investment in Kenya. Despite the improved business environment, the respondents noted that the country still lacks behind countries like Rwanda and Uganda in terms of annual direct foreign investment and therefore the country needs to improve its business operating environment especially the cost of production and security.

On the factors that are important in a country in order to attract direct foreign investment, the response from the respondents was unanimous that the country GDP level and its growth and the country population is an important factor in determining a country's attraction to direct foreign investment. A country's market size influences internal demand of the products and services and therefore if a country has a large market, then it will be able to attract foreign investors who will wish to capture such a market. The respondents also observed that in case the a country's GDP grows annually at a significant growth rate, then likewise the country will be able to attract FDI due to the increased purchasing power of the locals.

The availability of adequate and affordable workforce is yet another important parameter that influences the growth of foreign direct investment. The interviewees observed that a foreign investor will assess the available cost of labor in the country, skill available on certain technical duties and also the available level of education. They noted that certain investments, especially in banking, information technology, telecommunication and BPO are both capital and knowledge intensive and as a result, it is important for the country to provide the requisite knowledge as the foreign investor provides the capital. In addition, the respondents noted that it is not enough to provide the requisite knowledge but at the same time it should be sourced at a cheaper cost. This observation by the respondents is similar to that made by Bernama (2004) while studying the role of skilled workforce in attracting FDI in Malaysia in which he also noted that certain service sectors such as hypermarket retailing business in addition will require unskilled workforce and therefore whether the cost of labor is an important determinant may depend on the type of service industries under consideration.

The interviewees also observed that a number of changes have taken place in the recent past that have made the country attractive to the foreign investors. They pointed out that under the new constitutional dispensation, ownership of property by foreigners and locals alike has been enshrined in the constitution and the government of the day cannot compulsorily acquire such a property without adequate compensation. Several recourses have been availed in the constitution to aggrieved investors which include seeking a court redress both locally and in the East Africa Court of Justice. In addition, the respondents observed that Kenyan products have unrestricted entry into the United States of America market under African Growth and Opportunity Act (AGOA) for specified Kenyan products, market access to the Common Market for East and Southern Africa (COMESA) market of 400m people, East African Community (EAC) market of

150m people as well as the Kenyan products getting access to European Union, Japan and other European markets. Apart from the above markets that the Kenyan manufactured goods can access, the respondents also pointed out that in the last ten years Kenya has concluded Avoidance of Double Taxation Agreements with; United Kingdom, Germany, India, Canada, Norway, Sweden, Denmark, Zambia, France, South Africa, East African Community and Thailand, and is currently negotiating a number of others with various countries. In addition, it was also noted that Kenya has concluded Investment Promotion and Protection Agreements with France, Finland, Germany, Italy, Netherlands, Switzerland, China, Libya, Iran, Burundi and the United Kingdom, and is currently negotiating a number of others with various countries. All these steps have been undertaken by the Kenyan government in order to attract and retain foreign investors.

The licensing process of foreign investor has been hampering the level of FDI coming to the country over time. The respondents observed that after the country coming up with a one stop shop where all prospective investors –both local and foreign- seek advice and all requirements pertaining to licensing in the office. KenInvest facilitates approvals of prospective investment projects which have their details submitted on a prescribed application form issued by KenInvest.

The project must comply with the environment, health and security standards set in the pertinent Kenyan laws. KenInvest will then issue an Investment Certificate to all projects that are ready to start operation and have complied with the standards set by the relevant agencies such as the Attorney General Chambers and in some circumstances the security agencies in case the intended project is of concern. Thus it was noted that the slow licensing processes that is coupled with the high cost of registering property that is accompanied in most cases with heavy documentation should be reviewed by the government if it has to attract the foreign investment, n

On the question on what the government needs to do in order to attract the Foreign investment, the respondents pointed out that before the establishment of KenInvest, there appeared to be a loose link between the government and its related agencies with the foreign investors. They noted that many foreign investors perceived the government to be unfriendly and hostile to their operations. Because of this, the investors appreciated that the government through KenInvest has now changed the perceived view and instead has appreciated the role of FDI as a source of employment and as a contributor to the country's GDP. This has been achieved through KenInvest facilitating the interaction and providing an avenue of addressing their concerns.

4.4 Role of Kenya Investment Authority in Attracting the Foreign Direct Investment

This section of the interview guide aimed at establishing from the respondents, what role the KIA - as a government agency mandated to promote the foreign direct investment- undertake to achieve this mandate.

Towards this end the respondents observed that KIA has provided one-stop shop advantage office for investors in that all issues pertaining to local investment can be found in the office. In addition, KIA has developed a code that set forth guidelines on investment that enumerate the various investment incentives and mandate that all new projects should obtain before approval is granted. In addition, the interviewees observed that KIA has been continuously lobbying the government to harmonize investment regimes in all the East African Community countries and which will eventually aim to remove all tariff barriers between the states. In this way, the respondents pointed out that there will be further incentives to foreign investors to come to the local market since it will create an opportunity to access the larger East African Market.

In recognition of the challenge that comes from non-uniform investment policy between local and foreign investors, the interviewees noted that KIA has implemented investment rules that apply uniformly to both local and foreign investment. The uniform code was appreciated to have set clear guidelines for processing investment applications and will incorporate the means to ensure transparency and accountability. In addition, the investment guidelines developed by KenInvest has provided various incentives to investors, including procedures for obtaining such information and how the incentives are implemented. All this steps by KIA has helped in attracting foreign direct investment to the country.

The respondents also pointed out that the KIA has developed a resource-base centre to meet the information needs of potential investors. They observed that the Centre has been instrumental; they noted that in streamlining investment project application procedures and approvals in addition to organizing investment promotion activities and seminars, both in Kenya and abroad, aimed at sensitizing the international business community to the comparative advantages of investing in Kenya. In addition, the Kenya Investment Authority was pointed out as providing support to foreign and domestic companies intending to set up or expand in Kenya. This is achieved through the provision by the institution of fully integrated advisory services, assistance in acquiring licenses and requisite entry permits in addition to aftercare support. The interviewees pointed out that among the information in which the institution provides includes information on key regulatory factors; issuance of the Investment Certificate that facilitates immediate start of business; information on location factors and business opportunities; sector information and introduction to key sector networks and also provision of continued support to companies once they have been established.

The respondents also noted that the Kenya government ensures the protection of investments for both locals and foreign governments. Because of this, Kenya Investment Authority played an important role in the development of the various protection roles as well as encouraging the observance of the same during its implementation. It was found out that there exists a Foreign Investment Protection Act which guarantees against expropriation of private property by the government. In addition, the interviewees pointed out that that Kenya is a signatory of a number of international agreements such as member of Multinational Investment Guarantee Agency (MIGA) an affiliate of the World Bank which guarantees investors against loss of investment to political problems in host countries. In addition, the respondents also noted that that Kenya is a signatory to International Centre of Investment Disputes (ICSID) which is a channel for settling disputes between foreign investors and host governments. With all these protection the interviewees noted that the Kenya Investment Authority has endeavored to explain to both local and foreign investors the safeguards that exist locally in the protection of private property and which acts a source of an additional incentive to invest in the country.

On the issue of the licensing process for foreign investors, the respondents pointed out that Kenya Investment Authority has become a one stop shop for seeking all investment opportunities as well as facilitating the licensing process for investment in the country. They noted that up to five years ago, there existed many licensing requirement under different ministries and agencies. However, the KIA has lobbied the government to bring this entire requirement down to the current seven licenses. In addition, it is the KIA that follows for the prospective investor the licenses and keeps on updating them on the progress. This step has reduced instances of corruption during the licensing process and also reduced the licensing period to a maximum of two weeks. It was also noted that establishing a company in the country is quite straightforward and there are no separate

rules for foreign nationals. To register a company, certain mandatory documents such as the 'Memorandum of Association' and 'Articles of Association' must be filed with the Registrar of Companies within the Kenya State Law Office.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 SUMMARY OF FINDINGS

In summary, the study shows that the interviewees are aware of the role of Kenya Investment Authority in attracting direct foreign investment. The knowledge about the operations of the institution was exhibited by the internal respondents by virtue of all of them having worked in the institution for more than three years on average and also due to the fact that all of the interviewees were engaged in the day-to-day management and operations of attracting foreign direct investment. In addition, the respondents were found to be well versed with the subject matter of the study and all had solid academic background having attained a first degree. As a result of the above, the researcher felt that the results obtained from the respondents reflects the true position of the organization in attracting FDI.

It was found out in the study that with many countries in the region developing a conducive environment for foreign investment, it has become imperative that Kenya follows suit to become an investment destination of choice. It was found out that foreign investors are majorly concerned with the operating cost of their businesses and as well as the security of their investment. Thus, a country has to develop a secure business environment that is coupled with efficient communication infrastructure, labor cost, reduced inflation and available raw material. On the factors that influence the level of direct foreign investment in a country include a growing GDP level and market share, a country's market size.

Kenya has increasingly become attractive to FDI in the last 10 years and this has been due to an improved road and telecommunication infrastructure as well as more recently the enactment of a

new constitution that has put more safeguards in the protection of private property and thus no individual government can take a seizure policy without contravening the law. This they observed will help in attracting more direct foreign investment in Kenya

The licensing process of foreign investor has been hampering the level of FDI coming to the country over time. The respondents observed that after the country coming up with a one stop shop where all prospective investors –both local and foreign- seek advice and all requirements pertaining to licensing in the office. KenInvest facilitates approvals of prospective investment projects which have their details submitted on a prescribed application form issued by KenInvest. KIA has provided one-stop shop advantage office for investors in that all issues pertaining to local investment can be found in the office. In addition, KIA has developed a code that set forth guidelines on investment that enumerate the various investment incentives and mandate that all new projects should obtain before approval is granted. In addition, the interviewees observed that KIA has been continuously lobbying the government to harmonize investment regimes in all the East African Community countries and which will eventually aim to remove all tariff barriers between the states.

In addition, the Kenya Investment Authority has developed a resource-base centre to meet the information needs of potential investors. The Centre has been instrumental in streamlining investment project application procedures and approvals in addition to organizing investment promotion activities and seminars, both in Kenya and abroad, aimed at sensitizing the international business community to the comparative advantages of investing in Kenya. In addition, the Kenya Investment Authority was pointed out as providing support to foreign and domestic companies intending to set up or expand in Kenya.

The Kenya government has ensured protection of investments for both locals and foreign governments and towards this KIA has played an important role in the development of the various protection roles as well as encouraging the observance of the same during its implementation. It was found out that there exists a Foreign Investment Protection Act which guarantees against expropriation of private property by the government. In addition, the interviewees pointed out that that Kenya is a signatory of a number of international agreements such as member of Multinational Investment Guarantee Agency (MIGA) an affiliate of the World Bank which guarantees investors against loss of investment to political problems in host countries. In addition, the respondents also noted that that Kenya is a signatory to International Centre of Investment Disputes (ICSID) which is a channel for settling disputes between foreign investors and host governments. With all these protection the interviewees noted that the Kenya Investment Authority has endeavored to explain to both local and foreign investors the safeguards that exist locally in the protection of private property and which acts a source of an additional incentive to invest in the country.

5.2 Conclusion

From the research findings, some conclusions can be made about the study:

Attraction of direct foreign investment to a country is of importance to the host country in terms of creating employment and increasing the general economic development of the country. Therefore, it becomes imperative that the country establishes all necessary mechanism that will attract these investors. The necessary conditions such as efficient communication and road network should be availed and the cost of production also are made affordable through a supply of affordable labour, raw materials and power for running the factories. In addition, in the current globalized world,

there is need for a country to be a member of several multinational agencies that aim to protect foreign investment as well as establishing internal mechanism that will safeguard the interest of both foreign and local investors.

Apart from the establishment of ground conditions that will attract foreign investment, there is need also for a country to come up with an institution that will facilitate communication between a potential investor and the host country. Investors will prefer existence of a one stop shop where all inquiries will be directed as well as their licensing process be done. It is also important that the local institutions established to attract foreign investment be empowered to facilitate most of the licensing process and not have limited powers that will need them to consult other institutions that will lengthen process. The licensing process need to be streamlined in a way that a one stop shop of all the necessary licenses is done in the same office so that the process does not become a source of discouraging foreign investors.

5.3 Recommendation

The study recommends that the government directs more resources to the financing of the Kenya Investment Authority in order to fulfill effectively its mandate. The financing could take the form of seconding more qualified personnel in the institution, training and development of existing staff to equip them with the necessary know how that will facilitate effective performance of their duties. In addition funds should be availed for the institution to direct go outside the country approach individual investors that the country offers to their business. Indeed with Kenya being strategically located a relatively developed communication infrastructure and more skilled manpower, the country can tap on this competitive advantage to attract foreign investors.

The management of KIA needs to appreciate the importance of their institution in enhancement of the country's status as good destination of foreign investment. In this way they will need to lobby further the government to streamline all processes required for investing in the country. In addition, the current level of partnership between the institution and stakeholders need to be enforced to capitalize in all the strengths accruing from relationship. However, the institutions should be wary of investors whose demands might not be met.

5.4 Recommendations for Further Research

The study confined itself to Kenya investment Authority. This research should therefore be replicated in other government institution and local authorities that are in way or another engaged in facilitating direct foreign investment. In addition, a local research should be undertaken to establish the effectiveness of the various techniques employed by KIA to attract FDI and therefore facilitate ranking based on their importance.

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APPENDICES

Appendix I: Cover Letter

Caleb Salim Munyoki

School of Business, University of Nairobi

P.O. BOX 30197, Nairobi

August, 2011

Dear Respondent,

I am a postgraduate student at the University of Nairobi, School of Business. I am carrying out research on "The role of licensing process at KIA in attracting Foreign Direct Investment in Kenya". This is in partial fulfillment of the requirement for the degree of Master in Business Administration, (International Business) option Degree program at the University of Nairobi.

This study uses your organization as a Case of Study from which you have been selected as one of the respondent. The success of this research substantially depends on your help and co-operation.

I hereby request you to respond to questioner as honestly as possible and the best of your knowledge. The information provided will exclusively be treated with utmost confidence; neither your name nor any other details shall appear in my report.

Thank you in advance,

Yours sincerely,

Caleb S. Munyoki

(Student)

Dr John Yabs

(Supervisor)

Appendix II: Interview Guide.

Interview Questions:

The following sections provide sample questions to be used in evaluating the Role of Kenya Investment Authority in attracting Foreign Direct Investment in Kenya.

PART A: Background Information on the interviewees

1. What current position in the organization do you hold?
2. For how long have you been holding the current position?
3. Are you satisfied with the extent to which your organization has achieved in enhancing the growth of foreign direct investment in the country?
4. What is your highest level of education? What professional qualification have you attained?

PART B: Foreign Investment Environment in Kenya

5. How would you assess the investment environment in the country over the last 10 years? What changes have come out prominently in attracting the FDI? Please expound.
6. How much DFI has the country attracted in the last 10 years? In comparison to the earlier years has the trend over the period been positive or not? What has contributed to this trend?
7. What are some of the licensing requirements in the country? Have some of these licensing requirements have had an impact in the flow of FDI's?
8. What major factors influence the level of foreign direct investments?
9. What are some of the regulatory changes that have occurred recently that have impacted on the Kenya's level of foreign direct investment. Please expound.

10. What effect has the enactment of the new Constitution had on the level of foreign direct investment?
11. With the Kenya membership to several trading blocks, what effect has this move had on the level of FDI in the country?
12. In your own opinion, what role does the licensing process in the country have on the level of FDI?
13. Are there any conflicting roles in the various licensing agencies in the country in the process of attracting FDI?

PART C: Role of Kenya Investment Authority in Attracting the Foreign Direct Investment

14. How does KIA help in promoting local and foreign direct investment? Please expound.
15. What major changes has KIA enacted in the last five years that has led to the growth of FDI?
16. Has the organization become a one-stop shop for any investor? If not which other line ministries or authorities is the organization liaising with in attracting foreign direct investments?
17. What role does the organization play by influencing government ministries in the enactment of appropriate policies for investment in the country?
18. How will you describe the current licensing process of the FDI in the country? Can they be easily understood easily by investors?
19. Are there any restrictions on some types of businesses that foreign investors can't undertake in preference to local investors? If yes what types of businesses are these?
20. Have the local authorities licensing requirements in any way impeded foreign investment in the country?